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## **The Michigan Jobs & Investment Act** ***Transforming the SBT for the 21<sup>st</sup> Century***

When the Single Business Tax was enacted in 1975, Michigan was an industrial economic powerhouse – a world leader in the automotive, manufacturing, pharmaceutical and chemical industries, among others.

The concentration of the state's economy in a dominant automotive industry, the cyclical nature of that industry and the corresponding decline in state tax revenues, and the immediate budget crisis in 1975 fueled the shift from a mix of income, "intangible" and inventory-based taxes to a value added tax named the Single Business Tax (SBT). It promised, and delivered, the state a more stable revenue stream from a more broadly based tax while arguably spreading state business tax burdens across all types of businesses.

Since 1975 enormous changes have occurred in Michigan. Our economic base has diversified. Competitive pressures from other countries and states have intensified to attract our major job creators of the present and future. Business barriers to locating jobs where it is most economically advantageous are disappearing and these same job creators now face increased challenges in maintaining market share and the attendant jobs.

As these transformations occurred, the state's business tax structure has at best remained static. At worse, it has become corroded by special exemptions, credits and deductions that have been seldom, if ever, reviewed for effectiveness or efficacy.

Tax reform is not the entire solution to job creation – quality schools, well-trained workers and affordable health care are the rest of the job creation equation. This proposal encourages businesses to create jobs in Michigan.

The plan implemented through the Michigan Jobs & Investment Act would be the most significant business tax restructuring since the enactment of the SBT 30 years ago. It will help businesses that already call Michigan home to expand and persuade others to locate, headquarter and prosper in Michigan.

This act will provide broad-based cuts, create a simpler code, bring long-awaited fairness to the business tax structure and spur job creation and growth that the current business tax structure has failed to provide. And through this growth, we will support those elements that make Michigan a great place to live, work and raise a family: excellent education, affordable health care and safe communities.

## **The Existing Tax Structure**

Michigan's Single Business Tax was introduced in 1975, consolidating seven separate business taxes into one tax. It was designed to provide a reliable source of revenue to the state that would not fluctuate with the state's cyclic economy. The SBT is a value-added tax – the only one of its kind in the country – taxing the components that a company puts into making its products, including wages and profits.

Businesses also pay a personal property tax on machinery and equipment. While 36 other states have a personal property tax, 15 exempt manufacturing machinery and equipment.

The major complaints about our tax business structure are:

- The SBT overtaxes labor costs, while relying too little on profits for determining tax.
- Our high personal property tax discourages decisions to locate, expand or renovate facilities in Michigan.
- The "apportionment formula" - a way of computing the Michigan tax base for multi-state companies -- penalizes companies for having their headquarters in Michigan and discourages them from adding jobs here.

## **The Michigan Jobs & Investment Act Tax Cut Plan**

Governor Granholm has proposed a plan that will provide broad tax cuts, create jobs and simplify the business tax structure in Michigan.

**Under this plan, 77 percent of businesses that have a tax liability will see a cut.**

The plan would:

- Cut the standard SBT rate from 1.9% to 1.2% – *a 37 percent rate cut.*
- Cut the tax rate for small business from 2.0% to 1.2% – *a 40 percent rate cut.*
- Create a 35% personal property tax credit for manufacturing and research and development property.
- Provide a credit for research and development labor expenses.
- Increase the profit component of the tax base for corporations.
- Bring taxes on insurance companies more in line with the national average.
- Eliminate a series of special tax preferences within the SBT that have created inequities in the past.

Nearly 72,000 businesses that currently pay the SBT will see an immediate

reduction in their state tax burden. The Act also balances corporate business taxes by relying less on taxing labor and more on taxing profits. In other words, when profits are down, so are taxes.

For too long while manufacturing has served as the cornerstone of our economy,

"The Center for Automotive Research is delighted with the proposed, significant restructuring of Michigan's SBT that is fully consistent with the massive changes that are occurring in the business model of Michigan's manufacturing sector including the automotive industry. In effect this is a new pattern for tax policy that is consistent with being a full partner with the auto industry as it shifts to a new business model that emphasizes competition on a global basis. Clearly the SBT restructuring should have both a short and long term positive impact on automotive employment. The re-structuring also highlights the importance of being a good host state for the industry and is fair to those business investors, managers and employees have worked the hardest to make Michigan a successful and competitive region in which to work and live." – David Cole, chairman of the Center for Automotive Research

it has also shouldered a disproportionate share of the tax burden. Manufacturing accounts for 23% of our state's economy, and for the past five years, state and local taxes on durable manufacturing have averaged 24% of a businesses income,

nearly twice the average for all other companies (13.5%). To address this issue, personal property taxes on property used for manufacturing or research and development would be eligible for a 35% refundable credit. This will eliminate a tax disincentive to locate in Michigan.

Though Michigan is and must remain a manufacturing leader, we must also embrace and encourage economic diversity in the state as we work to stimulate the manufacturing sector. Often R&D companies have significant compensation costs, but not extensive property or manufacturing operations. These new credits will help us foster emerging technologies, the life sciences and homeland security businesses. This plan has a new tax credit for research and development companies based on those compensation expenses.

### **Transforming the SBT for the 21<sup>st</sup> Century**

While the revenue stability of SBT has proven beneficial, the costs to businesses have not been even across sectors or amongst all taxpayers. Various calculation methods and credits against the SBT have favored some taxpayers over others. And certain provisions in the SBTA have not kept up with modern business formations, resulting in tax advantages for certain business entities.

- Eliminating the special credit for unincorporated businesses
- Eliminating the special credit for telephone property taxes paid
- Eliminating the Excess Compensation Reduction
- Eliminating the Gross Receipts Reduction
- Treating compensation of employees leased from a professional employer organization as compensation of the client business
- Making small business credit eligibility independent of business organization or out-of-state affiliation.

- Increasing to 2 percent the premiums tax on insurance companies to bring it in line with most other states
- Eliminating the Special Property Tax Treatment for Commercial Rental Property

This plan will equalize tax burdens across sectors, as well as fund tax cuts for the most mobile of our industries and to small business.

This plan further balances the business tax burden by requiring insurance companies to shoulder a more proportionate share of taxes. Michigan's tax on insurers is the fourth lowest in the nation, yet Michigan consumers have not seen lower rates as a result. Currently, in-state insurers pay a tax equal to 1.07% of their premiums less credits. Out-of-state insurers generally pay the retaliatory tax, which is equal to what a Michigan-based insurer would pay if it were operating in another state. This tax plan adopts a 2% premiums tax for all insurers, putting Michigan in the middle of the pack of states that levy a premiums tax. (This tax does not apply to Blue Cross/Blue Shield, HMOs or self-insurance plans.)

### **Conclusion**

Fiscal responsibility requires tough choices. Michigan will benefit from this revenue neutral tax restructuring because it creates jobs, reorganizes business taxes in a way that results in a tax cut for 77 percent of Michigan's employers and makes the business tax fairer and simpler. Making the tax cut plan revenue neutral also ensures that Michigan's quality of life – good schools, affordable health care, and important public safety programs – is protected.